United States Court of Appeals

for the Second Circuit

APPELLEE'S PETITION FOR REHEARING EN BANC

75-7608

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P/S

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

IRVING SANDERS,

Plaintiff-Appellee,

—against—

LEON LEVY, *et al.*,

Defendants-Appellants.

EGON TAUSSIG,

Plaintiff-Appellee,

—against—

SIDNEY M. ROBBINS, *et al.*,

Defendants-Appellants.

MICHAEL SHAEV and RITA SHAEV,

Plaintiffs-Appellees,

—against—

ERIC HAUSER, *et al.*,

Defendants-Appellants.

UNITED STATES COURT OF APPEALS
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SECOND CIRCUIT

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF OF PLAINTIFFS-APPELLEES ON REHEARING *IN BANC*

WOLF POPPER ROSS WOLF & JONES
845 Third Avenue
New York, New York 10022
(212) 759-4600
Attorneys for Plaintiffs-Appellees

DONALD N. RUBY
ROBERT KORNREICH
MARIAN R. PROBST
Of Counsel

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UNITED STATES COURT OF APPEALS
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ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

BRIEF FOR PLAINTIFFS-APPELLEES ON REHEARING IN BANC

PRELIMINARY STATEMENT

This is an appeal by defendants under 28 U.S.C. § 1291 from an interlocutory order and decision of the

United States District Court for the Southern District of New York (Griesa, J.), determining that the above-entitled consolidated cases may be maintained as a class action under Rule 23(b)(3) of the Federal Rules of Civil Procedure on behalf of all persons who purchased shares of defendant Oppenheimer Fund, Inc. (the "Fund") between March 28, 1968 and April 24, 1970; that under the facts and circumstances of this case, the Fund shall bear the cost of culling out a list of the names and addresses of the class members from the Fund's computer tapes, and providing this list to plaintiffs, without prejudice to the right of said defendant at the conclusion of the action to make whatever claim it would be legally entitled to make regarding reimbursement by another party; and that the plaintiffs will be responsible for preparing and mailing the necessary notices, at their expense, with plaintiffs to have the option of sending them out in a separate mailing or including them in a regular mailing of the Fund, provided that the notices are sent only to class members and that plaintiffs pay in full the Fund's extra costs of mailing. The principal decision of the District Court, dated May 15, 1975, appears at page A-169 of the Appendix; and the Memorandum Order of the District Court, dated September 30, 1975, which essentially denied the motions for reargument, appears at page A-188 of the Appendix.

On June 30, 1976, a three-judge panel of this Court* unanimously affirmed the determination by the District Court that these cases may be maintained as a class action, but reversed (Hays, C. J., dissenting) the decision and order of the District Court directing the Fund to cull out the names and addresses of the class members from the Fund's computer tapes at the Fund's expense.

On September 14, 1976, this Court, pursuant to Rule 35 of the Federal Rules of Appellate Procedure, granted the plaintiffs-appellees' petition for a rehearing in banc of the aforementioned decision of the panel, insofar as it reversed the decision and order of the District Court, directing the Fund to cull out the names and addresses of the class members from the Fund's computer tapes at the Fund's expense.**

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* The panel consisted of Circuit Judges Hays and Mulligan and District Judge Palmieri, sitting by designation.

** Since the questions of appealability and class certification are not involved on this rehearing in banc, we have not discussed them in this brief. For some unexplained reason, defendants have included in their briefs submitted to the Court on this rehearing in banc factual information and arguments which pertain to the question of class determination. Since this question is not before the Court on this rehearing in banc, we do not believe that any response to the defendants' arguments on this point is warranted.

QUESTIONS PRESENTED

1. Are the discovery rules applicable to the identification of class members?

2. If the discovery rules are applicable, should the decision of the District Court requiring the Fund to bear the expense of culling out the names of class members from its computer tapes be disturbed by this Court absent the showing of an abuse of discretion?

3. Did the decision of the District Court requiring the Fund to bear this expense in this case constitute an abuse of discretion?

4. May notice costs be properly imposed by the district court upon a defendant where a fiduciary duty pre-existed between the plaintiff and the defendant, as in the instant case?

5. Did the District Court commit reversible error in the instant case in determining that the defendant Fund should bear the expense of culling out the names of class members from the Fund's computer tapes, assuming, *arguendo*, that this expense should be regarded as a notice cost, where there was a fiduciary relationship between the defendants and the plaintiff class and where, in addition, the added expenses of identifying the class members were necessitated by the defendants' request with regard to the definition of the class?

STATEMENT OF THE CASE

A. THE PLEADINGS

The three captioned actions were brought by plaintiffs representatively on behalf of themselves and other persons similarly situated who purchased shares of the Fund subsequent to March 15, 1968 (A-119),* and derivatively on behalf of the Fund (A-119), which is an open-ended investment fund registered under the Investment Company Act of 1940 with net assets in excess of $500,000,000 (A-131). These actions, which are based upon alleged violations of the Securities Act of 1933 (15 U.S.C. Section 77a et seq.), the Securities Exchange Act of 1934 (15 U.S.C. Section 78a et seq.) and the Investment Company Act of 1940 (15 U.S.C. Section 80(a) et seq.), and various rules promulgated thereunder, are brought against defendant Oppenheimer Management Corporation (the "Manager"), which is the investment advisor to the Fund and the general distributor of its shares; defendant Oppenheimer & Co., which owns all of the voting stock of the Manager, and the individual defendants, who are directors of the Fund. Some of the individual defendants are also officers of the Fund, officers and directors of the Manager and/or partners in Oppenheimer & Co.(A-119--A-171, A-10--A-46).

The complaints in these actions allege, in substance,

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* References are to pages of the Joint Appendix.

that the defendants caused the Fund to issue prospectuses and reports that were false and misleading, in that, among other things, they failed to state that the Fund would purchase "restricted" securities, and failed to describe the risks involved in such purchases. The complaints further allege, in substance, that the defendants caused the Fund to value improperly the restricted securities in the Fund's portfolio, thereby overstating the net asset value of shares of the Fund which were sold to the public, that the defendants caused the Fund to issue prospectuses and reports which were false and misleading in failing to disclose material information relating to the improper valuation of restricted securities in the Fund's portfolio, that the aforesaid conduct constituted a breach of fiduciary duties to the plaintiffs and the class and that, as a result of the foregoing, persons who purchased shares of the Fund subsequent to March 15, 1968 were caused to pay false and inflated prices for their shares of the Fund. The complaints further allege that, as a result of said improper valuation of restricted securities, the Fund was caused to pay the Manager excessive fees under its management agreement and to redeem shares at inflated prices. The plaintiffs seek to recover damages on behalf of the members of the class who paid excessive prices for their shares of the Fund*; and derivatively,

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* The total aggregate damages suffered by the class has been estimated to be in the area of $1,500,000. (A-151--A-153, A-159--A-160.)

on behalf of the Fund, to recover any damages sustained by the Fund and the profits made by the other defendants, including the excessive fees paid to the Manager. (A-10--A-46, A-119--A-120, A-171--A-172.)

The defendants have served amended answers denying any wrongdoing and asserting various affirmative defenses (A-47--A-82), including an alleged set-off against those members of the class who redeemed shares of the Fund since March 1968, for allegedly excessive amounts as a result of the overvaluation of restricted securities in the portfolio of the Fund. (A-56, A-71, A-80.) In addition, the defendants other than the Fund have asserted in their amended answers that, if they are liable to the class by reason of the overvaluation of restricted securities in the portfolio of the Fund, then "the Fund is liable to the defendants to the extent that the Fund has received funds from plaintiff and members of the Purchasing Class by reason of such overvaluation." (A-57, A-81.)

B. PRIOR PROCEEDINGS

The three captioned actions were commenced March 26, 1969, May 12, 1969 and June 18, 1969, respectively (A-119), and were consolidated for all purposes by order of the Court dated December 17, 1969. (A-20--A-21.)

Thereafter, the plaintiffs conducted extensive discovery proceedings, some of which, as indicated below, related

to the identification of class members and the method and cost of sending notice to the class, including the service of two sets of interrogatories, the examination of numerous documents and the oral examination of several officers and directors of the Fund and the Manager and the deposition of the Fund's transfer agent. (A-121, A-195.) The defendants also served interrogatories. which have been answered by the plaintiffs. (A-87--A-115.)

C. THE CLASS ACTION MOTION

On March 30, 1973, plaintiffs moved for an order pursuant to Rule 23(c)(1) of the FRCP declaring that this consolidated action may be maintained as a class action on behalf of all persons who purchased shares of the Fund during the period March 28, 1968 to April 24, 1970 (hereinafter referred to as "the class period"). (A-116--A-119.) In support of their motion for a class action determination, plaintiffs set forth information showing that all of the requirements for a class action under Rule 23(a) and (b)(3) of the FRCP were met. (A-118--A-128.)

Following the submission of the class action motion in March 1973 (and after this Court rendered its decision in Eisen v. Carlisle & Jacquelin, 479 F.2d 1005 (2d Cir. 1973), the plaintiffs, with the approval of the Court, conducted some discovery (principally the deposition of the Fund's transfer

agent) to obtain additional information relating to the composition of the class, the identification of class members and the method and cost of sending notice to the class. (Document 67, pp. 2, 3 and 5.)* The defendants did not object to the proposed discovery, notwithstanding the fact that defendants stated that it would require the Fund's transfer agent to "assemble and compile information and statistical data," (Document 66, pp. 1-3) except that the defendants argued that the discovery should be conducted by the use of written interrogatories, unless the plaintiffs paid, in the first instance, and subject to ultimate taxation of costs, the expenses of attendance of an attorney for each of the defendants at the place where the deposition was to be taken (Boston, Massachusetts), including reasonable attorneys' fee to be fixed by the Court. (Document 66, pp. 1-3; Document 68; Document 69.) The District Court, however, denied the defendants' application to require the discovery to be conducted by the use of written interrogatories and also denied the defendants' application to require the plaintiffs to pay, in the first instance, the expenses of attendance of an attorney for each of the defendants at the deposition. (A-195.)

Thereafter, the deposition of the Fund's transfer agent, pursuant to the Federal Rules of Civil Procedure, was taken, and the discovery disclosed the following information:

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* References are to documents listed in the "INDEX TO THE RECORD ON APPEAL," at pages A-1 to A-7 of the Appendix.

1. There were approximately 121,000 persons who purchased shares of the Fund during the class period (A-172, A-173);

2. The Fund currently had approximately 171,000 shareholders, of whom approximately 103,000 purchased shares of the Fund during the class period (A-145--A-174);

3. There were approximately 18,000 persons who purchased shares during the class period and were no longer shareholders of the Fund (A-174);

4. The names and addresses of the persons who purchased shares of the Fund during the class period could be culled out from the computer tapes of the Fund along with information indicating which of these persons were still shareholders of the Fund and which were not (A-149);

5. The cost of culling out the aforementioned information with respect to the names and addresses of class members, which would involve the use and programming of computers, would be approximately $16,000 (A-149);

6. There would be a charge of $0.01 per insert in connection with inserting the notice to class members in a regular mailing by the Fund to its shareholders (A-147).

In December 1973, after the foregoing information had been obtained, plaintiffs, in an affidavit submitted to the Court, modified their application relating to the definition of the class and requested that this action be maintained

as a class action on behalf of all persons who purchased shares of the Fund during the class period, and who, like the plaintiffs, were still stockholders of the Fund (A-143). This modification, it was noted, would simplify the issues in the case by eliminating, at least in part, the defense asserted by defendants in their amended answers, to the effect that defendants were entitled to a set-off against those persons who purchased shares in the class period but thereafter redeemed their shares for allegedly excessive amounts as a result of the overvaluation of restricted securities in the Fund's portfolio; it would facilitiate the distribution of any recovery to the class and, most importantly, as explained below, it would obviate the need for culling out the names and addresses of the class members and would thus reduce the expenses involved in connection with the further prosecution of the case as a class action (A-143--A-144).

The definition of the class sought by plaintiffs would have obviated the need for culling out the names and addresses of the members of the class from the Fund's computer tapes in order to give notice to the class, since, if all of the members of the class were current shareholders of the Fund, the class notice could then be enclosed in a regular mailing by the Fund to all of its shareholders, which would include all the class members. Thus, the method of giving notice proposed by the plaintiffs would have provided for actual

individual notice by mail to all members of the class apprising them of the pendency of the action and of their right to request exclusion from the class pursuant to the provisions of Rule 23 (A-145--A-148).

Moreover, since the proposed class was defined by the plaintiffs with precision (all persons who purchased shares of the Fund during the class period and were still shareholders of the Fund on a specified date prior to the mailing of the class notice), there would be no problem in entering a judgment in the action, whether favorable or not to the class pursuant to Rule 23(c)(3), describing the persons who were bound by the judgment (A-146).*

Plaintiffs stated that they would pay for the costs of preparing the necessary notices and would pay for any extra costs involved in mailing the class notice in the manner proposed by them, including the cost of inserting the notice in a regular mailing by the Fund to all its current stockholders (A-147). It was estimated that these costs, which the plaintiffs were prepared to pay, would be approximately $5,000. (A-147) If it were necessary, however, to ascertain the names and addresses of the class members in order to give notice to the class, the total costs involved in connection with giving

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*In the event of a recovery in the action, the names and addresses of class members would, of course, be ascertained in connection with the distribution of the recovery (A-146).

notice would be in excess of $20,000 (A-147). The plaintiffs indicated that, if they were required to pay at that time the costs of identifying the class members as well as the costs of sending notice to the class, they would not continue prosecution of the action as a class suit (A-147, A-149).

The defendants opposed the definition of the class sought by plaintiffs which limited the class to persons who were still stockholders of the Fund, presumably because it would limit the res judicata effect of this action (A-174--A-175). However, since, at the same time, the defendants themselves sought to limit the class to persons who purchased shares of the Fund prior to April 25, 1969 (A-137), it would appear that, in seeking to have the class defined so as to include persons who were no longer shareholders of the Fund (which would make it necessary to ascertain the names and addresses of the class members in order to give notice to all members of the class), the defendants were interested in increasing the expenses involved in connection with giving notice to the class in the hope that the district court would impose these added expenses upon the plaintiffs and that this would prevent the action from proceeding as a class suit.

Defendants also objected to the distribution of the class notice in the manner proposed by the plaintiffs (by directing the notice specifically to those shareholders of the Fund who purchased during the class period and enclosing

the notice in a regular mailing of the Fund to all of its 171,000 shareholders), claiming that this method would result in the notice being received by aproximately 68,000 shareholders of the Fund who were not members of the class, and that this would somehow have an adverse affect on the Fund, including allegedly precipitating a flood of redemptions by these shareholders (A-138--A-141). In response to defendants' objections, plaintiffs pointed out that, since 1970, the Fund had apprised its shareholders in its proxies, prospectuses and annual reports, no fewer than 13 times, of the pendency of this action, and the nature of the claims alleged herein, and of the fact that, in the opinion of their counsel, and counsel for the Manager, the suits have "no legal merit." Plaintiffs contended that the defendants had not made an adequate showing to support their claims of alleged harm, and that defendants' claims were motivated by a desire to maximize the costs involved in an effort to prevent the action from proceeding as a class suit, and that defendants had not raised any valid objections to the method of giving notice proposed by the plaintiffs (A-148--A-150).

All of the issues raised by plaintiffs' motion for a class action determination were fully explored and briefed by the parties and were carefully considered by the District Court prior to its decisions on the motion. On several occasions, the Court requested additional information and briefing

with respect to various matters, including the definition of the class, the appropriate method of giving notice to the class in this case, the effect of the decision by this Court in Eisen v. Carlisle & Jacquelin, 479 F.2d 1005 (2d Cir. 1973) ("Eisen III"), and the appropriate allocation in this case of the cost of culling out a list of class members from the Fund's computer tapes under the discovery rules and in light of all the facts and circumstances in the case. (Documents 33, 34, 40-43, 45, 49-52, 70, 78, 79, 82-87, 89-98, 101-111, 113).

DECISION AND MEMORANDUM
ORDER OF THE DISTRICT COURT

On May 15, 1975, Judge Griesa rendered a decision determining that the consolidated action may be maintained as a class action under Rule 23(b)(3) of the FRCP on behalf of all persons who purchased shares of the Fund between March 15, 1968* and April 24, 1970 (A-170).** The District Court found that the "requirements of a class action under Rule 23 are clearly met in the present case" (A-172).

With respect to the definition of the class, the method of giving notice to the class and the allocation of

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* The starting date of the class period was modified in Judge Griesa's memorandum order of September 30, 1975, on consent of the parties, to March 28, 1968 (A-189).

** The Court rejected the defendants' claim that the class should be limited to persons who purchased prior to April 25, 1969 (A-176--A-177).

the costs of culling out from the Fund's computer tapes a list of the names and addresses of the class members, the District Court rendered a decision which took into account the respective positions and proposals urged by the parties with respect to these matters, and constituted the Court's considered judgment as to what would be a fair overall disposition of the matter, based upon the particular facts and circumstances in this case (A-170--A-178). The Court agreed to define the class as requested by the defendants to include those persons who were no longer shareholders of the Fund and agreed to defendants' related request that notice not be sent out in the manner proposed by the plaintiffs by including the notice in a regular mailing to all current shareholders of the Fund, but that the notices be sent only to those current shareholders of the Fund who are class members, thereby necessitating the identification of the specific names and addresses of class members in order to send notice to the class (A-176--A-178). With regard to the matter of culling out the names and addresses of the class members from the Fund's computer tapes, the Court determined that it would be appropriate, on the basis of the facts and circumstances of this case, that this expense, which was necessitated by the defendants' requests with regard to the definition of the class and the method of giving notice to the class, be the responsibility of the defendants, and the Court indicated that the Fund should bear the cost of culling out

from its computer tapes the names and addresses of the class members in this case. In reaching this decision, the Court stated:

> "Moreover, with respect to the cost of culling out the list of class members, I am ruling that this is the responsibility of defendants. Whether this would be the correct allocation in other cases, I do not attempt to say. But here the expense is relatively modest and it is the defendants who are seeking to have the class defined in a manner which appears to require the additional expense." (A-175.)

The Court further determined that the plaintiffs would be responsible for preparing and mailing the necessary notices to the members of the class at their expense. (A-170, A-178.)

After all parties moved for reargument, the Court, in a memorandum order dated September 30, 1975, denied essentially all of the motions for reargument. The Court indicated in its memorandum order that the cost of culling out the list of class members shall be borne by the Fund without prejudice to the right of this defendant at the conclusion of the action to make whatever claim it would be legally entitled to make regarding reimbursement by another party;* and that, as to the mailing of notices, plaintiffs are to have the option of: (a) sending them out in their own mailing, or (b) including

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* In its motion for reargument, the Fund had requested the Court to clarify its ruling as to which of the defendants are to bear the cost of culling out the names and addresses (footnote continued on next page)

them in a regular mailing of the Fund, provided that the notices are sent only to class members and that plaintiffs pay in full the Fund's extra cost of mailing, including the cost of segregating the envelopes going to the class members from the envelopes going to other Fund shareholders (A-189--A-190).

The Panel Decision

In its decision dated June 30, 1976, the three-judge panel of this Court unanimously held that the order of the District Court was appealable and that the granting of class action status was proper.

The majority of the panel (Judge Hays dissenting), reversed the order of the District Court directing the Fund to cull out the names of class members from the Fund's computer tapes at the Fund's expense. In reaching this decision, the majority decided that the discovery rules were inapplicable in determining whether the District Court had committed reversible error in imposing upon the Fund the cost of culling out the

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* (continuation of footnote from preceding page)

and, that, if the Court required the Fund to bear such cost, its ruling should set forth that the payment at this time is an advance and that there has been no determination of the question of contribution. (Document 106, p. 7.) It may be noted that the Court had, in fact, already indicated, in its decision of May 15, 1975, that the Fund was to be responsible for this cost (A-170). The Manager, in its motion for reargument, asserted that, "[i]f the defendants are to bear the cost of preparing lists, such cost should be advanced in the first instance by the Fund, as provided in the Court's opinion (at p. 2)." (Document 102, p. 5.)

names of class members from the Fund's computer tapes. The majority also held that the "usual rule" set forth by the Supreme Court in Eisen v. Carlisle & Jacquelin, 417 U.S. 156 (1974) ("Eisen IV"), and by this Court in Eisen v. Carlisle & Jacquelin, 479 F.2d 1005 (2d Cir. 1973) ("Eisen III"), that the plaintiff must bear the cost of notice, must be applied to the instant case, notwithstanding the fact that a fiduciary duty pre-existed between the plaintiffs and the defendants, including the Fund, and that the District Court had found that the expense of culling out the names and addresses of class members from the Fund's computer tapes was attributable to defendants' request with regard to the definition of the class.

In his dissenting opinion, Judge Hays stated:

> "The majority's decision, ostensibly predicated on the Supreme Court's decision in Eisen v. Carlisle & Jacquelin (Eisen IV), 417 U.S. 156 (1974), uncritically treats a discovery issue as notice and indiscriminately applies a rule appropriate to arm's-length relationships to the fiduciary relationship between the parties herein." (Slip Opinion, p. 4591.)

Judge Hays indicated, in his dissenting opinion, that identification of class members is ascertainable by discovery and governed by the rules applicable thereto, that the allocation of the expense involved in obtaining this information rests within the sound discretion of the District Court and should not be disturbed absent a showing

of abuse of discretion and that the District Court did not abuse its discretion in imposing upon the Fund the cost of culling out the names of class members from the Fund's computer tapes.

Judge Hays further stated that, even if the expense involved in identifying the members of the class must be regarded as a notice cost rather than a discovery expense, the "usual rule" should not be applied in the instant case, since there was clearly a fiduciary duty between the defendants and plaintiff class, and that, under these circumstances, the District Court may properly impose said cost upon the Fund in this case.

In reaching his conclusion, Judge Hays noted that the application of the "usual rule" to the instant case would create "a serious potential for insulating fiduciary breaches from redress" and that the majority decision would "close yet another door to the class action procedure." (Slip Opinion, pp. 4593, 4597.)

POINT I

THE DISCOVERY RULES ARE APPLICABLE TO THE IDENTIFICATION OF CLASS MEMBERS. ACCORDINGLY, THE DECISION OF THE DISTRICT COURT REQUIRING THE FUND TO BEAR THE EXPENSE OF CULLING OUT THE NAMES OF CLASS MEMBERS FROM ITS COMPUTER TAPES SHOULD NOT BE DISTURBED BY THIS COURT, UNLESS IT CONSTITUTED AN ABUSE OF DISCRETION. THE DECISION OF THE DISTRICT COURT IN THIS CASE WAS NOT AN ABUSE OF DISCRETION.

The majority of the panel stated that the cost of

discovering the names of class members did not differ in kind from the cost of printing the notice and of procuring, stuffing and posting the envelopes, and thus the discovery rules were inapplicable in determining whether the District Court committed reversible error in imposing the costs of identification upon the defendants in this case (Slip Opinion, pp. 4587, 4588). The majority's analysis of this issue is, we submit, unsound. As Judge Hays correctly observed in his dissenting opinion:

> "When identification is sought information allowing a party to proceed with his suit is at the core of the request. Thus, in purpose and effect such a request is not different in kind from other requests for information routinely made during discovery. That a suit will be unable to proceed absent identification does not vitiate the validity of characterizing identification as a product ascertainable by discovery and governed by the rules applicable thereto. A contrary view clearly is belied by the common practice of establishing jurisdiction by means of discovery." (Slip Opinion, p. 4593.)

The majority would distinguish discovery of information relating to the identification of the class members from discovery of information generally, presumably because the former relates to class action requirements in the case. Carried to its logical conclusion, the majority's decision would make the discovery rules inapplicable to other matters (in addition to the identification of class members) that are germane to the requirements for maintaining a suit as a class

action under Rule 23, such as the description of the class, the numerosity of class members, etc. Indeed, the defendant Manager, in its brief, contends that information "which is sought for the purpose of enabling plaintiffs to prosecute [the suit] as a class action rather than in their individual capacities does not bear at all on the substantive issues of the litigation, but is entirely collateral thereto...," and is, therefore, "outside of the scope of discovery." (Defendant Manager's brief, pp. 31, 33.) This contention is, however, clearly unsound and unfounded in either the federal rules or in case law. Burstein v. Slote, 12 FR Serv.2d 577 (S.D.N.Y. 1968); Branch v. Reynolds Metals Co., 17 FR Serv.2d 494 (E.D. Va. 1972); Dickerson v. United States Steel Corp., 18 FR Serv.2d 554 (E.D.Pa. 1974); Wolfson v. Solomon, 54 F.R.D. 584 (S.D.N.Y. 1972); Appleton Electric Co. v. Advance-United Expressways, 494 F.2d 126 (7th Cir. 1974); Shapiro v. Merrill Lynch, 70 Civ. 3653 (S.D.N.Y. July 11, 1974) (unreported decision).

In Burstein v. Slote supra, the Court, in denying defendants' motions for protective orders denying the right of plaintiffs to take defendants' depositions with respect to the nature and extent of the class, stated:

> "Since amended Rule 23 has been in effect, oral examination with respect to such subject matter has been permitted in this District. See Herbst v. Able, 278 F.Supp. 664 (SDNY 1967); Crabtree v. Hayden, Stone Inc., 67 Civ. 3968 (January 16, 1968, April 5, 1968); Kronenberg v. Hotel Governor Clinton, Inc.,

66 Civ. 1297 (October 28, 1966). In view of the mandatory notice requirements of Rule 23(c)(2) (once an action is judicially determined to be maintainable as a class suit), and no indication present that plaintiffs are abusing the discovery rules so as to harass defendants, plaintiffs are permitted to inquire of defendants on oral examination as to the names of the purchasers of securities of Manufacturers Credit Corp. and its related entities, the amounts purchased by each investor, and the identity of the person or corporation through whom the securities were purchased.

"Plaintiffs, of course, may not use this information to notify other members of the putative class of the pendency of these actions unless and until they are denominated class actions by court order...." (Emphasis supplied.) 12 FR Serv.2d at 579-580.

In Branch v. Reynolds Metal Co., supra, the Court overruled defendant Reynolds' objections to the plaintiffs' interrogatories which were directed to the class allegations in the action, stating:

"Reynolds' first ground, if sustained, would place plaintiffs' counsel in the anomalous position of not being able to sustain its class contentions for lack of evidentiary support, yet unable to adduce such support by reason of its inability to prove class standing. Placing counsel in this bootstrap dilemma would be a perversion of the liberal spirit of the federal discovery rules." (Emphasis supplied.) 17 FR Serv.2d at 195.

In Dickerson v. United States Steel Corporation, supra, the Court held that the plaintiff was entitled to discovery under the federal rules as to the size and character of the potential class even before determination of the class action motion. The Court said:

> "...[T]here is nothing either in the wording or the spirit of these rules which prevents the Court from allowing discovery on the class action question...." 18 FR Serv.2d at 555.

In Wolfson v. Solomon, supra, the Court required the defendants to supply to the plaintiffs, pursuant to Rule 34, any information they have on how many persons bought certain stock in the over-the-counter market during a specified period of time, and, thus, would be members of the class.

In Appleton Electric Co. v. Advance-United Expressways, supra, the Court held that the District Court did not abuse its discretion in requiring the defendant carriers to provide the names and addresses of shippers who were members of the class, notwithstanding the testimony by defendants as to the difficulties and costs involved in furnishing this information. In reaching this conclusion, the Court noted:

> "...[I]n view of the broad discovery of class members permitted in this Circuit..., it would indeed be anomalous to place restrictions on discovery in this refund case." 494 F.2d at 138.

Thus, it is clear that discovery has been allowed by the Courts pursuant to the federal rules in connection with the requirements for maintaining a suit as a class action under Rule 23. Indeed, if this were not the case, plaintiffs would find it impossible, in most cases, to demonstrate to the Court that the requirements of Rule 23 had been satisfied.

The American College of Trial Lawyers (the "College"), in its amicus brief, takes a less extreme view than the defendant

Manager with respect to the question of whether information relating to the class action requirements of Rule 23 can be obtained under the discovery rules ,but one that is equally unsound. The College acknowledges that the plaintiff may be entitled to certain discovery under the federal rules with respect to the class action requirements under Rule 23, such as the number of class members, but the College contends that the names of class members are not a proper subject for discovery under the federal rules. We submit that the distinction urged by the College is an arbitrary one, which finds no support in either the federal rules, in case law or in logic. If plaintiffs are permitted, under the discovery rules, to obtain information as to the parameters or scope of the class, the number of class members, etc., it would be clearly arbitrary to hold that plaintiffs may not obtain information under the discovery rules as to the names of the class members.

Furthermore, the fact that Rule 23(c)(2) provides that "the Court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort," does not, as defendants contend, indicate that the identification of class members is not subject to discovery. If this were true simply because the identification of class members is referred

to in the same paragraph of Rule 23(c)(2) as the provisions for giving notice to the class, it would also follow that information relating to whether the members of the class "can be identified through reasonable effort" or what is "the best notice practicable under the circumstances," which are also referred to in the same paragraph of 23(c)(2), would not be obtainable through discovery. Yet, in this very case, discovery was permitted by the District Court, without objection by the defendants, with respect to these matters and other matters relating to the method and cost of sending notice to the class. If such information may be obtained through discovery, there is no justifiable reason for concluding that information relating to the names and addresses of class members is not subject to discovery; and the courts have specifically recognized, as indicated above, that, because of the mandatory notice requirements of Rule 23(c)(2), a plaintiff should be allowed to obtain information pursuant to the discovery rules as to the names of class members. See Burstein v. Slote, supra; Appleton v. Advance-United Expressway, supra.*

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* In Popkin v. Wheelabrator Frye, Inc., CCH Fed. Sec. L. Rep. ¶ 95,411 (S.D.N.Y. 1976), cited by the Fund in its brief (pp. 19-20), Judge Cannella indicated that Rule 23(c)(2) requires plaintiff to make a "reasonable effort" to identify the members of the class. If plaintiffs, however, could not conduct discovery of defendants to obtain information with respect to the names of class
(continued next page)

To conclude, as the majority of the panel did, and as the defendants urge herein, that information relating to the identity of class members is outside the scope of discovery and that the discovery rules are not applicable in determining the allocation of the expenses relating thereto is, we submit, wholly unfounded, and is inconsistent with the federal rules and with applicable case law.

The defendant directors, in their brief, urge a slightly different contention than that of the Manager or the College, but one that is also unfounded. The defendant directors acknowledge that discovery of the names and addresses of class members may now be permissible under the federal rules, but they urge that, "since the discovery here sought is solely for the purpose of enabling plaintiffs to fulfill their obligations under Rule 23, the cost of such discovery should clearly be borne by the plaintiffs." (Defendant directors' brief, p. 7.) Thus, the defendant directors urge that the cost of all discovery relating to the class action requirements under Rule 23 should be borne by the plaintiffs, and that the district courts, in allocating the expenses of discovery, should be required to differentiate between

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(footnote continued from previous page)

members, the plaintiffs, in the usual case, might not be able to send to the members of the class the notice required by Rule 23(c)(2).

information that is relevant only to the class action requirements of the case and information that is relevant to the merits generally. We submit that no such distinction is either compelled or intended by Rule 23, by the federal rules of discovery or by Eisen III or Eisen IV, and that such a distinction is both inappropriate and inadvisable. In Eisen IV, the Supreme Court held that the cost of notice is, in the usual case, the responsibility of the plaintiff "as part of the ordinary burden of financing his own suit." Eisen IV, supra, at 179. The expenses involved in the discovery of information, however, have not been automatically regarded as part of the ordinary burden of a party of financing his own suit, but rather the allocation of such expenses has traditionally rested within the sound discretion of the district court. We submit that matters pertaining to discovery of information, whether they relate to class action matters or to the merits of the case, should be left to the sound discretion of the district courts, and that the district courts' determination with respect to the allocation of discovery expenses should be disturbed only upon a showing that there has been an abuse of discretion.

None of the cases cited by the defendants supports their contention that the discovery rules are inapplicable to the identification of class members or that the plaintiffs

must bear the discovery expenses involved in identifying the class members. For example, in Grad v. Memorex Corporation, 61 F.R.D. 88 (N.D. Ca. 1973), the plaintiff had agreed to pay for the cost of identifying the class members prior to the mailing of notice. There is nothing in the Grad case which indicates that it would be an abuse of discretion for the district court to impose upon a defendant the expenses involved in identifying the class members from its records. In Berland v. Mack, 48 F.R.D. 121 (S.D.N.Y. 1969), Judge Mansfield required the defendant, at its expense, to furnish to the plaintiffs' counsel a list of the names and addresses of the members of the class. In B&B Investment Club v. Kleinerts, Inc., CCH Fed. Sec. L. Rep. ¶ 94,451 (E.D. Pa. 1974), the Court cited, with approval, the procedure in Berland v. Mack, supra, for identifying the members of the class. In Herbst v. International Telephone & Telegraph Corporation, District Court opinion reprinted in Appendix, 495 F.2d 1308 (2d Cir. 1974), the Court, notwithstanding the fact that it imposed the cost of notice upon the plaintiffs, required the defendants to provide certain listings or materials in their possession relating to the identification of class members. In State of Illinois v. Harper & Row Publishers, 301 F.Supp. 484 (N.D. Ill. 1969), the plaintiffs were state and municipal governments who brought actions on behalf of public libraries, school districts and boards of education within their jurisdiction.

Thus, the information relating to the identification of the members of the class was clearly within the possession of the plaintiffs, and thus it was not necessary for them to conduct discovery of the defendants in order to identify the members of the class.

The cases cited by the College in its brief (p. 13) to the effect that the district courts have directed plaintiffs to arrange for and pay for the cost of sending special notices to brokerage firms and other nominees in order to identify class members whose shares are held in "street name" are irrelevant to the issue before the Court. Plaintiffs do not contend that the defendants must bear all of the expenses involved in identifying all the members of the class irrespective of whether the information pertaining to the identity of the class members is in the possession of the defendants. In the cases cited by the College, the information regarding the identity of class members was not being sought from the defendants, as in the instant case, but rather from brokérage firms. Thus, these cases are not relevant to the situation in the instant case, where the information relating to the identification of class members is contained in the Fund's computer tapes. The determination of whether the discovery expenses involved in obtaining this information from the defendants should be shifted from the Fund to the plaintiffs, as the defendants urge in this case, should rest, we submit, within the sound discretion

of the district court.

It is well recognized that the district court has wide discretion in matters of discovery, including the allocation of expenses relating thereto, and that the discretionary judgment of the district court in the realm of discovery should not be disturbed absent a showing of abuse of discretion. Baker v. F & F Investment, 470 F.2d 778 (2d Cir. 1972), cert. denied 411 U.S. 966 (1973); H. L. Moore Drug Exchange, Inc. v. Smith, Kline & French Laboratories, 384 F.2d 97 (2d Cir. 1967); Harvey v. Eimco Corp., 28 F.R.D. 381 (E.D. Pa. 1961).*

Under the discovery rules, parties may be required to furnish information calling for investigation or accumulation of data, even though a considerable burden or expense may be involved. If the information sought is relevant and material, a responding party, under the federal discovery rules, in order to shift the expense to the other side, must show not only that the request for information is burdensome but that

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* In Brown v. Thompson, 430 F.2d 1214 (5th Cir. 1970), the Court, in reviewing a discretionary determination by the district court in a discovery matter, observed:

> "The judges of the Court of Appeals might well feel that under like circumstances they would have exercised the judicial discretion in a manner different from that in which it was exercised by the trial court. But this is not a basis for reversing the determination of the trial court. The test is whether there has been an abuse of that discretion...."

the burden is so excessive as to be unreasonable or oppressive. 4A Moore's Federal Practice, ¶ 33.20; Caldwell Clements, Inc. v. McGraw Hill Publishing Co. 12 F.R.D. 531, 538 (S.D.N.Y. 1952); U.S. v. Nysco Laboratories Inc., 26 F.R.D. 159, 161-162 (S.D.N.Y. 1960); American Oil Co. v. Pennsylvania Petroleum Products Co., 23 F.R.D. 680, 683 (D.R.I. 1959). Specifically, with regard to the obligation of a responding party under the federal rules to provide information which is contained in computer tapes, Professors Wright and Miller state in their well-known treatise:

> "The responding party who is required to prepare a printout or otherwise make the data reasonably usable for the discovering party must ordinarily bear the expense of doing this. He can shift the cost to the discovering party only on a showing under Rule 26(c) that justice so requires in order to protect himself from 'undue burden or expense'" 8 Wright & Miller, Federal Practice and Procedure, Section 2218 at page 659.

Thus, parties may be required to undergo substantial burdens and expense in furnishing information under the discovery rules so long as the burdens are not unreasonable or oppressive. We submit that to require the defendants in this case to pay for the cost of culling out a list of class members from the Fund's computer tapes can hardly be regarded as "unreasonable" or "oppressive" when it is the defendants themselves who have made it necessary to obtain this information.

None of the cases cited by the defendants dealing with the discovery rules (most of which focus on Rule 33) show that the District Court abused its discretion in this case in refusing to shift the burden of the expenses involved in identifying class members from the Fund to the plaintiffs. These cases do not set forth any hard-and-fast rules with regard to the allocation of discovery expenses. Rather, the cases indicate that the matter is to be determined within the discretion of the court upon the facts and circumstances presented by the particular case. In passing, it may be noted that in none of these cases was it the defendant, as in the instant case, who had necessitated the need for the information.

Judge Hays, we believe, correctly observed in his dissenting opinion that Rule 34, which governs production of computerized information, is more appropriate to the instant case than Rule 33 and that there are serious dangers involved in restricting the discretion of the district court in dealing with the discovery of computerized information. Judge Hays noted:

> "It is somewhat disingenuous to focus, as the majority does, on Rule 33 which governs interrogatories rather than the Rule more specifically designed to govern computerized information. Since the disclosing party has opted to keep his records on computer tapes, there is good reason to allow the district court the usual discretion as to costs of retrieving information from those tapes lest discovery be obstructed by irretrievably burying information to immunize business activity from later scrutiny." (Slip Opinion, pp. 4593-4594)

In concluding that the District Court had not abused its discretion in the instant case, Judge Hays, after referring to the treatise by Professors Wright and Miller, which is quoted above, stated:

> "While the authors [Professors Wright and Miller] suggest that courts should be sensitive to the expense involved since the disclosing party may be obliged 'to engage in fairly sophisticated electronic manipulation and analysis,' id., expense remains an issue properly resting within the sound discretion of the district judge. Under the facts of this particular case the district judge did not consider the costs of processing the defendant's tapes an 'undue burden or expense.' It is not our practice to disturb the discretionary judgment of a district court in the realm of discovery absent a showing of abuse, see, e.g., Baker v. F&F Investment, 470 F.2d 778 (2d Cir. 1972), cert. denied, 411 U.S. 966 (1973); H.L. Moore Drug Exchange, Inc. v. Smith, Kline & French Laboratories, 384 F.2d 97 (2d Cir. 1967), and discovery of class members should provide no exception. Imposing the cost of culling out the names of members of the class upon the Fund involved no abuse of discretion. The district court, finding this expense attributable to defendants' objections to plaintiffs' efforts to define a subclass minimizing expenses, cf. Eisen IV, supra at 179, n.16, did not commit reversible error in refusing to shift this burden to plaintiffs. Moreover, the order below specifically notes that it is 'without prejudice to the right of this defendant [the Fund], at the conclusion of the action, to make whatever claim it would be legally entitled to make regarding reimbursement by another party." (Slip Opinion, pp. 4594-4595).

The contention by the College that it would be constitutionally improper for the District Court to require the Fund, in the instant case, to bear the expenses involved in identifying the class members and that this would

constitute a "confiscation" of the defendants' property is difficult to understand. It is surely not constitutionally improper, nor a confiscation of the defendants' property for the district court to require a defendant to bear the discovery expenses involved in identifying the class members. Nor is it constitutionally improper to require a defendant in an appropriate case not covered by the "usual rule" to pay the costs of giving notice to the class. If this were not the case, then the statements by the Supreme Court in Eisen IV, and by this Court in Eisen III, that there may be exceptions to the usual rule would be meaningless.

The College's further contention that the plaintiffs should be required to post a bond in connection with the cost involved in identifying the class members, is equally without merit. First of all, the College has cited no authority in support of this novel proposition that a party should be required to post a bond to secure the payment of certain expenses which the district court, in the course of the litigation, has determined should be imposed upon an adverse party. This would clearly be contrary to accepted practice.* Furthermore, in the instant case, the

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* See Appleton Electric Co. v. Advance United Expressway, supra, where the Court, in discussing the question of notice costs, stated:
(continued next page)

determination by the District Court, as noted by Judge Hays, specifically provides that it is without prejudice to the right of the Fund at the conclusion of the action, "to make whatever claim it would be legally entitled to make regarding reimbursement by another party." Thus, the Fund may, at the conclusion of the action, seek contribution from the other defendants, or if the defendants prevail in this action, it may seek to have these expenses taxed against the plaintiffs pursuant to Rule 54(d) of the federal rules. The matter of taxation of costs would then rest within the sound discretion of the district court. National Transformer Corp. v. France Manufacturing Co., 215 F.2d 243 (6th Cir. 1954); Busch v. Masiello, 55 F.R.D. 72 (S.D.N.Y. 1972); 10 Wright and Miller, Federal Practice and Procedure, § 2676.**

If the plaintiff in a class action were required to post a bond (which can be very burdensome and expensive) in connection with discovery expenses or notice costs which the

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* (footnote continued from page 35)

> "...although the plaintiff has not volunteered that it will ultimately bear the costs, there is no requirement that a party agree to bear costs which a court could ultimately assess against his opponent." (Emphasis in original text.) 494 F.2d at 136.

** Contrary to the assertion made in the briefs of the defendants and the College, the plaintiffs have not stated that "they will not and cannot reimburse defendants if defendants ultimately prevail." College brief, pp. 18-19. The

district court has properly imposed upon the defendant, as in the instant case, it would unquestionably further discourage and impede the prosecution of class actions. Before the Court -- to use Judge Hays' words -- rushes "to close yet another door to the class action procedure", it is well to keep in mind the important function served by class actions in insuring the effective enforcement of the federal securities laws, in deterring corporate officials from violations of their fiduciary duties and in vindicating the rights of individuals whose claims are too small to justify legal action but which are of a significant size if taken as a group. Green v. Wolf Corporation, 406 F.2d 291 (2d Cir. 1968); Escott v. Barchris Construction Corp., 340 F.2d 731 (2d Cir. 1965); Berland v. Mack, 48 F.R.D. 121 (S.D.N.Y. 1969); Dolgow v. Anderson, 43 F.R.D. 472 (P.D.N.Y. 1968).** (Footnote appears on page 38.) In Green v. Wolf Corporation, supra, this Court

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* (footnote continued from page 35) record indicates that the plaintiffs, in December 1973, indicated to the Court that they would not continue the prosecution of the class action if they were then required to pay the expenses involved in identifying the class members. They, of course, did not say at that time that if the defendants were ultimately to prevail, and if the district court, in its discretion, taxed these expenses against the plaintiffs, they would not and could not meet their legal obligations at the conclusion of the case. Of course, if the plaintiffs prevail, the question of taxing these costs against the plaintiffs would be academic. Moreover, whether these expenses would be taxed against the plaintiffs, even if the defendants were successful, is speculative, since the district court is given broad discretion in these matters. In any event, the question of taxation of costs is not now before this Court and must await further developments.

underscored the importance of the class action device in cases involving violations of the securities laws, stating:

> "...'[t]he ultimate effectiveness of the federal remedies when the defendants are not prone to settle may depend in large measure on the applicability of the class action device. 3 Loss, Securities Regulation 1819 (2d Ed. 1961).'" 406 F.2d at 295.

In Escott v. Barchris, supra, this Court said:

> "...[T]here is a particular need for the representative action as a device for vindicating claims which, taken individually, are too small to justify legal action but which are of significant size if taken as a group." 340 F.2d at 733.

In Berland v. Mack, supra, the Court stated:

> "...[W]e are mindful of declarations by the Court of Appeals for this Circuit to the effect that the rule must be liberally construed with a view to enhancing the use of class actions as a means of vindicating rights of absent members who are unable, for one reason or another, personally to prosecute; and that the device is particularly suitable for use in suits charging violations of the anti-fraud provisions of the federal securities acts, which have been increasingly recognized as a private policing weapon supplementing governmental administrative action." 48 F.R.D. at 125.

** From p. 37) It would appear that the College, in its brief (p. 5, fn.), would have this Court disregard these important functions of class actions in considering the matters presently before the Court. The College would have this Court approach these questions on the basis that the "preeminent purpose" of the class action device under Rule 23 is "to concentrate in a single forum multitudinous claims which otherwise would be litigated separately in many state and federal courts." (Emphasis in the original text.) We believe that the various contentions raised herein by the College, as well as the defendants, which would, if accepted by the Court, seriously discourage the prosecution of class actions and undercut their effectiveness, essentially ignore the important functions served by class actions.

We respectfully submit that the discovery rules should be applicable in determining whether the District Court committed reversible error in this case in requiring the Fund to bear the costs of culling out the names of class members from its computer tapes, that the determination of the District Court should not be disturbed absent a showing of abuse of discretion and that, based upon the facts and circumstances in this case, the District Court did not abuse its discretion.

POINT II

THE DISTRICT COURT DID NOT COMMIT REVERSIBLE ERROR IN DETERMINING THAT, UNDER THE FACTS AND CIRCUMSTANCES OF THIS CASE, THE FUND SHOULD BEAR THE EXPENSE OF CULLING OUT THE NAMES OF CLASS MEMBERS FROM THE FUND'S COMPUTER TAPES, EVEN IF THIS EXPENSE SHOULD BE REGARDED AS A NOTICE COST.

While apparently recognizing that, under the principles set forth in Eisen III and Eisen IV, there may be exceptions to the "usual rule" that the plaintiff must bear the costs of notice, the defendants as well as a majority of the panel have construed these exceptions so restrictively as to make them essentially meaningless. They would, thus, transform the usual rule into a much more pervasive and inflexible rule than was intended by either Eisen III or Eisen IV. The majority and the defendants have also misapprehended, we submit, in certain important respects, the proper role of the district court in connection with the matters involved in this case. The proper exercise of discretion by the district courts, particularly in cases, like the instant one,

involving unusual facts and circumstances and fiduciary relationships between the parties, is essential, we submit, to insure the effective use of the class action procedure and to achieve fair and equitable results.

A.

The District Court May Properly Impose Notice Costs upon a Defendant where a Fiduciary Duty Pre-existed between the Plaintiff and the Defendant, as in the Instant Case.

Both this Court in Eisen III (479 F.2d at 1009, n. 5) and the Supreme Court in Eisen IV (417 U.S. at 178) noted that the usual rule that the plaintiff must bear the cost of notice may not apply "where a fiduciary duty pre-existed between the plaintiff and the defendant * * * ." Eisen IV, supra, at 178. The majority of the panel, while recognizing this possible exception to the usual rule, construed this exception too narrowly and based its determination that this exception should not apply in the instant case upon certain erroneous factual assumptions. The majority appears to have limited the exception to situations where the defendant is essentially in the position of a corporation in a shareholder's derivative suit or is a public service monopoly (Slip Opinion, pp. 4582-4583). In Eisen IV, however, the Supreme Court cited Dolgow v. Anderson, 43 F.R.D. 472, 498-500 (E.D.N.Y. 1968), as an example of a case that might present such an exception to the usual rule. See Eisen IV, supra, at 178, fn. 15. In Dolgow, the defendant was neither a public service

monopoly nor in the position of a corporation in a derivative suit. Indeed, in Dolgow, which, like the instant case, was a class action brought by plaintiffs on behalf of purchasers of securities, the defendants were in essentially the same position as the defendants in the instant case. In the portion of the opinion in Dolgow specifically cited by the Supreme Court in Eisen IV, the Court indicated that a defendant corporation may be required to bear the cost of notice based upon the "fiduciary duty owed to purchasers of stock by the corporation...." Dolgow, supra, at 498.

It may be noted, in passing, that all three of the grounds referred to by the Court in Dolgow, in the portion of the opinion in Dolgow specifically cited by the Supreme Court in Eisen IV, as providing a basis for requiring the defendant corporation to pay the cost of notifying the members of the class, are present in the instant case, i.e., the fiduciary relationship between the defendants and the plaintiff class; the advantages to the defendants of a judgment with res judicata effect against the class, and the ability to bear the cost. In the instant case, the Fund, as indicated below, has a fiduciary obligation to the members of the class; the class has been defined, as requested by the Fund and the other defendants, to include persons who are no longer shareholders of the Fund so that the defendants will have the advantage of a judgment with broader res judicata

effect,* and the Fund obviously has a greater ability to bear the cost than the plaintiffs in this case. It should also be noted that, while the Court in Dolgow was discussing the question of whether the aforementioned grounds justified imposing the entire cost of notice upon the defendants, in the instant case all that the District Court has required the Fund to bear is the cost involved in culling out the names of class members from the Fund's computer tapes, a cost that has been necessitated by the defendants themselves. The District Court has required the plaintiffs to pay all the costs of preparing the notice and any extra costs of mailing involved in sending out the notice

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* See Fund brief, p. 11, where the Fund specifically states that it opposed the plaintiffs' definition of the class, which would have excluded persons who were no longer shareholders of the Fund because of the prejudice "to the Fund by a possible multiplicity of new suits."

The College, in its brief (pp. 15-16), suggests that the typical defendant in a class action is not really interested in the res judicata effect of a class action judgment but is much more interested in having the class action dismissed so that the defendant will avoid the risk of an adverse judgment in favor of the class. We have no doubt that this is true in most cases and that the supposed interest of the defendant in having the class defined more broadly to secure the res judicata effect, is simply a ploy by the defendant (along with its opposition to less expensive methods of giving notice to the class) to make it more difficult and costly for the plaintiffs to prosecute the suit as a class action. We submit, however, that these tactics should not be sanctioned by the Court and that, where the defendants seek to increase the costs involved in prosecuting the suit as a class action in the hope that this will result in the suit's being discontinued as a class action, the district court should be able, as in the instant case, to require the defendants to bear the extra costs necessitated by them so that the suit may be maintained as a class action and so that the defendants will not have escaped liability to the class without even a determination on the merits.

in a regular mailing of the Fund to the class members, including the cost of segregating the envelopes going to the class members and the envelopes going to other shareholders. In addition, under the District Court's decision the plaintiffs would bear the full cost of sending out the notice to those members of the class who were no longer shareholders of the Fund.

It is evident that neither the Supreme Court nor this Court, in noting that the usual rule requiring the plaintiff to bear the costs of notice under Rule 23 may not apply "where a fiduciary duty pre-existed between the plaintiff and the defendant," could have intended to limit the fiduciary relationship exception to situations involving shareholder's derivative suits, since a shareholder's derivative suit is not even a class action under Rule 23, but rather is covered by Rule 23.1, which does not require that a notice be sent out, comparable to the notice required by Rule 23(c)(2), apprising shareholders of the pendency of the action and the right to opt out. Rule 23.1, on the contrary, requires that notice be sent out only in connection with a dismissal or compromise of the action.

There can be no doubt that there was a fiduciary relationship between the plaintiffs and the defendants in the instant case (Slip Opinion, p. 4596; dissenting opinion). Even the majority of the panel appears to have recognized that the defendants had fiduciary duties to the plaintiffs and the class

(Slip Opinion, pp. 4583-4584). In this connection, Judge Hays stated, in his dissenting opinion:

> "Unquestionably the relationship between the Fund shareholders and the defendants herein is of a fiduciary nature. As one court has observed, the Investment Company Act 'impose[s] fiduciary obligations of the highest order upon persons who control investment companies.' Securities and Exchange Commission v. Advance Growth Capital Corp., 470 F.2d 40, 55 n.21 (7th Cir. 1972). See, Investment Company Act of 1940, 15 U.S.C. §80a-35. So too, '[t]he Investment Advisors Act of 1940...reflects a congressional recognition "of the delicate fiduciary nature of an investment advisory relationship. ..."' Securities and Exchange Commission v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 191 (1963), quoting 2 Loss, Securities Regulation (2d ed. 1961) at 1412. It is the breach of these fiduciary duties which is at the core of this suit." (Slip Opinion, p. 4596)

The majority, nevertheless, disregarded the fiduciary relationship between the parties herein and compelled the application of the usual rule to the instant case, based upon two grounds, both of which, we submit, are unfounded. First, the majority asserts that many of the considerations pointed to in justification for shifting the costs of notice from the plaintiff to the defendant in Dolgow and in Eisen v. Carlisle & Jacquelin, 52 F.R.D. 253, 264-270 (S.D.N.Y. 1971), such as the strength of plaintiff's case and the ability of the defendant to bear the costs, have been shown to be inappropriate (Slip Opinion, p. 4584). It does not follow, however, simply because it has been determined that these considerations will not justify imposing the costs of notice upon the defendant, that other considerations, such as the existence of

a fiduciary relationship between the plaintiffs and the defendants, which both Eisen III and Eisen IV have indicated may justify the imposition of notice costs upon the defendants, should be disregarded. The inevitable result of the approach urged by the defendants herein, and taken by the majority, is the creation of a hard-and-fast rule that the plaintiff in a class action must pay the cost of notice, irrespective of legitimate considerations like those in the instant case, which, as this Court and the Supreme have indicated, may properly influence the Court in determining who should bear the costs of notice.*

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* We do not contend, on this appeal, that the district court must, in all cases where there is a fiduciary relationship between the defendants and the plaintiff class, impose the costs of notice upon the defendants. There need not be a rigid rule. The district court, however, should have discretion in those cases not covered by the "usual rule," such as where the defendants have a fiduciary duty to the plaintiff class, to determine the proper allocation of the costs of notice based upon the facts and circumstances of the case. The statements by Judge Canella in Popkin v. Wheelabrator-Frye, Inc., CCH Fed. Sec. L. Rep. ¶ 95,068 (S.D.N.Y. 1975) cited by the defendants, are, we believe, inconsistent with the decisions by the Supreme Court and by this Court in Eisen, insofar as they suggest that, under the decisions by this Court and the Supreme Court in Eisen, a rigid rule must be applied in imposing the costs of notice and that the plaintiff must pay the costs of notice in all cases without exception. In any event, all that is before the Court on this appeal is whether the District Court could properly impose the costs of identifying the class members (assuming arguendo that this is a notice cost), upon the Fund in the instant case, where there is a fiduciary relationship between the Fund and the plaintiff class and where these costs were necessitated by the defendants' request with respect to the definition of the class.

The majority also bases its decision that the fiduciary relationship exception should be disregarded and the usual rule should apply in the instant case upon the mistaken assumption that the Fund is not a party to the class action claims and has no direct interest in the outcome of said claims and thus is too remotely involved to have notification costs imposed upon it (Slip Opinion, pp. 4583-4584). The majority, however, has overlooked the fact that the defendants other than the Fund have asserted cross-claims against the Fund in their amended answers, alleging that, if they are liable to the class by reason of the overvaluation of restricted securities in the portfolio of the Fund, then the Fund is liable to them to the extent that the Fund has received funds from the class by reason of such overvaluations. (A-57, A-81).* Thus, contrary to the assumption by the majority, the Fund

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* The assertion by the defendant Fund in its brief (p. 22) that the other defendants in the case have only "asserted affirmative defenses in the nature of an offset against the Fund as to any damages to which these defendants may be held liable to the Fund" is clearly erroneous. It is evident from the answers of these defendants that they are seeking to hold the Fund liable to them to the extent that they are held liable to the class, by reason of the overvaluation of restricted securities in the portfolio of the Fund. It is also evident that while the plaintiffs had demanded damages from the Manager and the directors rather than the Fund, the complaint does allege a violation of fiduciary duty by the Fund to the plaintiffs and the class since the Fund is alleged to have issued false prospectuses and reports, to have improperly valued restricted securities in the Fund's portfolio and to have sold shares of the Fund to the plaintiffs and the class at inflated net asset values.

does have a direct interest in the outcome of the class action claims.**

The reasons for not applying the usual rule in cases like the instant one, where a fiduciary relationship exists between the defendants and the plaintiffs, have been cogently set forth by Judge Hays, as follows:

> "When the defendants assumed their positions with the Fund they knew, or clearly should have known, that the law imposes very stict standards upon their conduct. Their relationship to the plaintiff class is one of trust; the entire scheme of our investment company and advisor regulation is predicated upon that trust being respected inviolate. A breach of a fiduciary duty traditionally has been considered a much graver transgression than, for example, breach of a contractual duty....In cases involving fiduciaries,...the usual rules traditionally have been modified to insure that the trust

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** The majority also notes, in support of its decision, that "[w]e may not assume that non-class member shareholders would approve of the Fund underwriting these expenses for the benefit of other shareholders." (Slip Opinion, p. 4583.) If the matter were put to a vote, however, it is reasonable to assume that a majority of the Fund shareholders would approve of the Fund's bearing these expenses, since approximately 60% of the Fund's shareholders are members of the class (A-145--A-174). The defendant directors, in their brief (p. 13), assert that the Fund and its directors "cannot properly prefer one group of Fund shareholders over another" and that it would be "inappropriate to use Fund assets to finance an action brought for the personal benefit of less than all the present Fund shareholders." Yet, it is interesting to note that the directors of the Fund and the Manager, who are defendants in this action and who control the operations of the Fund, have compelled the use of the Fund's assets to contest the claims in this class action against the defendants, notwithstanding the fact that they contend that no relief is being sought against the Fund and the fact that a recovery would benefit approximately 60% of the Fund's shareholders.

relationship is not abused. The norms appropriate in the context of arms-length bargaining are simply inapposite in the fiduciary context. Thus, the usual rule should not apply to preclude class action when to do so creates a serious potential for insulating fiduciary breaches from redress." (Slip Opinion pp. 4596-4597.)

B.

The District Court did not Commit Reversible Error in Determining that the Fund should Bear the Costs of Culling out the Names of Class Members from its Computer Tapes, since the Added Expenses were Necessitated by the Defendants' Requests with Regard to the Definition of the Class.

As indicated above, this Court, in Eisen III, specifically stated that courts may find justification, depending upon the particular facts and circumstances involved, for holding that the plaintiff is not obligated to pay the costs of notice.*

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* This Court stated in Eisen III:

"Nor did we decide or intend to say [in Eisen II, 391 F.2d (2d Cir. 1968)] that in all cases or under all circumstances plaintiffs in class actions are or must be required to defray the cost of giving the various notices specified in amended Rule 23. This is an action to recover money damages for alleged violations of Section 4 of the Clayton Act and Section 6 of the Securities and Exchange Act of 1934. It is not a derivative stockholder's action asserting a cause of action in favor of a defendant corporation, which regularly sends communications to all the stockholders and may be said to owe its stockholders certain fiduciary duties, nor a case where a public utility corporation which regularly sends monthly bills to its current customers has been held to have overcharged its customers and the class suit is

In the instant case, consistent with the principles set forth by this Court in Eisen III, the district court determined that, under the particular facts and circumstances of this case, the Fund should bear the cost of culling out from its computer tapes the names of class members. The District Court stated:

> "Moreover, with respect to the cost of culling out the list of class members, I am ruling that this is the responsibility of defendants. Whether this would be the correct allocation in other cases, I do not attempt to say. But here the expense is relatively modest* and it is the defendants who are seeking to have the class defined in a manner which appears to require the additional expense." (A-175; emphasis supplied.)

In reversing the District Court, the majority, notwithstanding the foregoing express statement by the District Court that the added expenses of culling out the names of class

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* In referring to the additional costs as "relatively modest," the District Court was no doubt mindful of the fact that $16,000 was not a great burden to bear for the Fund which has over $500,000,000 in net assets, in consideration for having the Court define the class and having the notice distributed in a manner preferred by the defendants.

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> brought to compel a refund. There may be other similar examples of class actions in which, depending on the circumstances of particular cases, courts might find justification for holding that a representative plaintiff was not obligated to defray the cost of giving the notices required by amended Rule 23. We do not attempt any enumeration. It must be recalled that the provisions for notice in amended Rule 23 were intended to to comply with constitutional requirements. See Advisory Committee's Note, 39 F.R.D. 69, 107." (Emphasis Supplied) 479 F.2d at 1009, fn. 5.

members were necessitated by the defendants, appears to have concluded that these expenses were not attributable to "partisan demands" on the part of the defendants but rather to reasons "unrelated to the interests of the defendants" (Slip Opinion, pp. 4586, 4587).* In support of their conclusion, the majority p[illegible] to the fact that the District Court indicated, in its opinion, that the definition of the class proposed by the plaintiffs would involve an arbitrary reduction in the class, and it ruled in favor of the defendants in defining the class. From this the majority argues that the additional identification costs cannot be viewed as expenses necessitated by partisan demands on the part of the defendants, and accordingly it was improper for the District Court to impose these costs upon the defendants. What the majority overlooks is that the District Court's rulings in this case with regard to the definition of the class, the method of giving notice and the allocation of the costs of culling out the names of class members from the computer tapes of the Fund were obviously interrelated and reflect the District Court's considered judgment as to a fair overall disposition of this matter, taking into account the respective positions and proposals urged by the parties with

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* Contrary to the majority, Judge Hays was of the view that the District Court had, indeed, found that these additional expenses were "attributable to defendants' objections to plaintiffs' efforts to define a subclass minimizing expenses..." (Slip Opinion, p. 4594).

respect to these matters. Whether the District Court would have refused to define the class as proposed by the plaintiffs had it not also determined that the Fund should be responsible for the additional costs involved in defining the class in the manner sought by the defendants is questionable. The majority appears erroneously to assume that it would have been legally improper for the District Court to have overruled the defendants' objections and to have defined the class as sought by the plaintiffs. We submit, on the contrary, that the district court could have defined the class as proposed by the plaintiffs consistent with the principles of Rule 23,* but determined instead, in the

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* There is substantial authority indicating that the courts should employ the full measure of discretion under Rule 23 to allow classes to be defined by the plaintiffs so as to permit utilization of the class action procedure, Dolgow v. Anderson, 43 F.R.D. 472, 492 (E.D.N.Y. 1968), even where "the restriction on the scope of the class appears arbitrary." State of Illinois v. Harper & Row Publishing, Inc., 301 F. Supp. 484, 494 (N.D. Ill. E.D. 1969). In Dolgow, which involved an action by purchasers of Monsanto stock, the Court noted that it would probably not be difficult or expensive to notify the members of the class who were still holders of Monsanto, and indicated that, if notice to those persons who were no longer stockholders of Monsanto would create a problem, "it might be necessary to limit the class to include only those who could be provided with notice from current Monsanto shareholder lists." 43 F.R.D. at 498. See also Eisen IV, supra, at 179, n. 16, indicating that the class might be redefined by the plaintiff and the scope of the class reduced so as to minimize the costs of notice.

The method of giving notice proposed by the plaintiffs would also have satisfied the provisions of Rule 23 and the requirements of due process, since it would have provided actual individual notice by mail to all members of the class as defined by plaintiffs. See Eisen III; Eisen IV; Advisory

exercise of its discretion, to grant the defendants' request with regard to the definition of the class and to require defendants to bear the additional expenses involved in defining the class as sought by them. We further submit that, from a fair reading of the entire opinion of the District Court, it is evident that the District Court took into account the "partisan

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Committee Notes, 39 F.R.D. 69, 107; Mullane v. Central Hanover and Trust Company, 339 U.S. 306, 70 Sup.Ct. 62 (1950). Furthermore, the insertion of a notice in a regular mailing by a corporate defendant to its shareholders in order to reduce the cost of giving notice to the class, as proposed by plaintiffs, has been favorably referred to by the courts. Zachary v. Chase Manhattan Bank, 52 F.R.D. 532 (S.D.N.Y. 1971); Dolgow v. Anderson, supra, at 500; Popkin v. Wheelabrator- Frye, Inc., CCH Fed. Sec. L. Rep. ¶ 95,0688 (S.D.N.Y. 1975); Eisen IV, at p. 180, fn. 1 (concurring and dissenting opinion). It is not improper either for a notice to be distributed to a group, only some of whom will qualify as members of the class. See In re Antibiotics Antitrust Action, 333 F.Supp. 291, 294, where the notice was distributed on the basis of occupant mailing lists; and Berland v. Mack, 48 F.R.D. 121, (S.D.N.Y. 1969), where the notice was also sent to some people who were not members of the class in order to insure that all members of the class would receive the notice. There is nothing in Rule 23 or in any of the Eisen decisions which prohibits the sending of notice to a group of persons that is larger than the actual class or which indicates that it is improper for the Court to minimize the costs of notice consistent with the requirements of Rule 23 and due process. None of the cases cited in the Manager's Brief (pp. 48-49) indicate that it would have been improper to have included the class notice in a regular mailing by the Fund to all of its current shareholders. The fact that the members of the class would not have been identified by name prior to sending notice to the class does not preclude the maintenance of the action as a class suit. Dolgow v. Anderson, 43 F.R.D. 472, 492-493 (E.D.N.Y. 1968), Fischer v. Kletz, 41 F.R.D. 377, 384 (S.D.N.Y. 1966), so long as the provisions of Rule 23 and the requirements of due process have been satisfied.

demands" of the defendants in deciding upon the definition of the class and in determining to require the Fund to bear the additional expenses involved in culling out the names of the class members from its computer tapes.

The majority decision also misconceives the proper role of the district court in giving notice to the class under Rule 23(c)(2). In seeking t support its determination that the District Court could not properly impose the added expense of identifying class members upon the defendants, the majority concludes that the defendants' concern, with respect to sending the notice to shareholders of the Fund who were not class members (as proposed by plaintiffs), was legitimate, notwithstanding the fact that the Fund shareholders had been advised of the nature and pendency of this suit 13 times since 1970, in proxies, prospectuses and annual reports, because "we think that notice of that type...would have a far milder impact than a separate communication (though mailed with other papers) composed by the plaintiffs, giving a detailed explanation of the claims and without a denial of merit...." (Slip Opinion, pp. 4586-4587; emphasis supplied.) In reaching this conclusion, the majority completely ignores the fact that Rule 23(c)(2) provides that the court shall direct notice to the class and that the form and content of this notice is not determined by the plaintiffs but rather by the court. Thus, the district court could fully protect the legitimate interests of the defendants in passing

upon the form of notice in the case. Accordingly, it was premature for the majority to have concluded, as it did, that the defendants' concern that the mailing of the notice to non-class members would have an adverse effect upon the Fund was legitimate.* We believe that the majority's approach on this point further evidences a misconception as to the proper role of the district court in connection with matters relating to the maintenance of class actions under Rule 23.

The determination by the District Court in this case is also consistent with the approach taken by the Court in Berland v. Mack, supra, where Judge Mansfield ordered that, if notice by publication were requested by either party in addition to individual notice by mail (the defendant had so requested), then a copy of the notice would be published and the cost of notice by publication would be borne by the party

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* The District Court did not decide, as the defendant Manager erroneously claims in its brief (pp. 46, 50), that the method of giving notice proposed by the plaintiffs was improper or that the defendants' claims of harm resulting from giving notice in this matter were in any sense well-founded. In this connection, see Miller v. Mackey International Inc., 452 F.2d 424 (5th Cir. 1971), where the Court rejected a claim by the defendant that sending a class notice to the shareholders of the defendant, who had already been apprised of the litigation in prospectuses and letters sent by the defendant to them, would "seriously injure the financial position" of the corporation. It is interesting to note that, contrary to the assertions of the defendant Manager, the defendant Fund expressed the view in its brief which was submitted to the panel (p. 19) that the district court, by its rulings in this case, in effect approved the propriety of the method of giving notice proposed by the plaintiffs.

requesting it. By the same token, if defendants insist upon specifically identifying the members of the class so that the class can be defined and notice can be given in a manner preferred by them, then the defendants should also assume responsibility for the extra costs incident to having the class defined and notice given in the manner requested by them.

The District Court determined that, under the particular facts and circumstances of this case, where there was a fiduciary relationship between the defendants and the plaintiff class, and where the added expenses of identifying the class members were necessitated by the defendants' requests with regard to the definition of the class, it would be appropriate to have the defendants and, in particular, the Fund bear the cost of culling out the names of the class members from the computer tapes of the Fund. We submit that the decision of the District Court is fully compatible with Rule 23 and with the principles set forth in Eisen III and in Eisen IV and represents a proper exercise of the role of the district court in handling the complicated and varying problems presented by class actions.

CONCLUSION

For the reasons stated herein, this Court should affirm the order and decision of the District Court requiring the Fund to bear the costs of culling out the names of class members from its computer tapes.

Respectfully submitted,

WOLF POPPER ROSS WOLF & JONES
Attorneys for Plaintiffs-Appellees
Office and P. O. Address
845 Third Avenue
New York, New York 10022
(212) 759-4600

DONALD N. RUBY
ROBERT M. KORNREICH
MARIAN R. PROBST

Of Counsel

Service of 2 copies of this within
Brief is admitted this
19 day of October 1976

ATTORNEYS FOR Defts-Appells. Oppenheimer Fund Inc.
Management Corp. etc.

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WEISMAN, CELLER, SPETT, MODLIN,
WERTHEIMER & SCHLESINGER

Atty's for Deft-Appl. Oppenheimer Fund, Inc

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Attorney for Edmund T. Delaney + Emanuel Celler

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